TACTICAL ASSET ALLOCATION COMMITTEE MONTHLY COMMENTARY

JULY 2018

FIERA CAPITAL

In June, investors attempted to reconcile some encouraging signs of global economic strength with heightened trade tensions and some hawkish undertones from several major central banks - all of which added to financial market volatility during the month. The global trade dispute intensified after President Trump's ramped-up protectionist threats were swiftly met with vows for retaliation from America's closest allies – all but threatening to derail the strongest global expansion since 2011. Meanwhile, central banks are slowly stepping away from the proverbial punchbowl. The Federal Reserve raised interest rates in June and adopted a more aggressive path to future normalization, while the European Central Bank announced that its asset purchase program will come to a close in 2018 after several years of balance sheet expansion.

FINANCIAL MARKET DASHBOARD

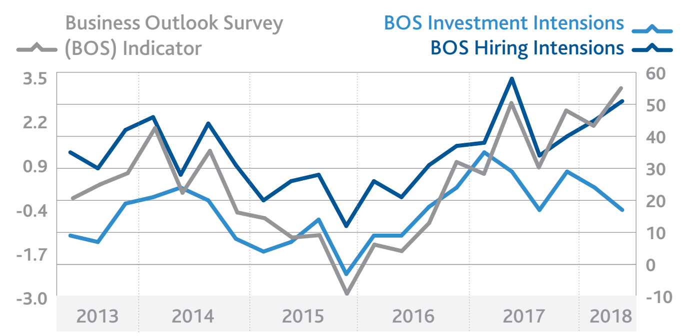
	JUNE 29, 2018	JUNE	YTD	1 YEAR
EQUITY MARKETS		% PRICE CHANGE (LC)		
S&P 500	2,718	0.48%	1.67%	12.17%
S&P/TSX	16,278	1.35%	0.42%	7.22%
MSCI EAFE	1,959	-1.39%	-4.49%	4.01%
MSCI EM	1,070	-4.57%	-7.68%	5.81%
FIXED INCOME (%)		BASIS POINT CHANGE		
US 10 Year Bond Yield	2.86	0.2	45.5	55.6
US 2 Year Bond Yield	2.53	10.1	64.5	114.7
CA 10 Year Bond Yield	2.17	-7.6	12.3	40.6
CA 2 Year Bond Yield	1.91	-0.4	22.5	81.1
CURRENCIES		% PRICE CHANGE		
CAD/USD	0.76	-1.33%	-4.29%	-1.30%
EUR/USD	1.17	-0.08%	-2.67%	2.26%
USD/JPY	110.76	1.78%	-1.71%	-1.45%
COMMODITIES		% PRICE CHANGE		
WTI Oil (USD/bbl)	74.15	10.61%	22.72%	61.06%
Copper (USD/pound)	2.95	-3.72%	-10.59%	9.34%
Gold (USD/oz)	1,254.50	-3.51%	-4.19%	0.98%

Global equity markets posted some mixed results in June. North American indices led the way, with the S&P 500 posting its third consecutive monthly advance, while US small cap stocks jumped to new record levels. And despite stalled-out NAFTA negotiations, the S&P/TSX hit an all-time high in late June – thanks to an impressive comeback in the energy space. In contrast, European bourses stumbled after President Trump threatened to impose tariffs on European car imports, while emerging market stocks plummeted alongside the mounting trade rift between Washington and Beijing, while higher US interest rates also spurred outflows from developing-nation assets.

In fixed income markets, the US 10 year treasury yield was virtually unchanged in June as investors gauged some conflicting forces at hand. While lingering trade uncertainties have weighed on sentiment and sent investors flocking to the safety of US treasuries, the resurgence in crude prices and some encouraging signs of life on the inflation front helped to place a floor under bond yields. Meanwhile, the short-end of the curve backed-up as market expectations converged towards the Federal Reserve's accelerated path to policy normalization. Finally, corporate spreads widened as appetite for risk soured in the environment of heightened geopolitical anxieties - though high yield outperformed on the back of a recovery in the energy sector.

In currency markets, the greenback advanced versus its G10 peers and capped its best quarter since 2016. Notably, the euro declined even after the ECB announced an end to its asset purchase program later this year. Instead, the central bank managed to soften its stance somewhat and conveyed that interest rates will remain unchanged until the back-half of 2019. Meanwhile, the yen retreated after the Bank of Japan downgraded its inflation assessment and reiterated that the end of ultra-stimulative support is nowhere in sight. Finally, brewing trade tensions and widening interest rate differentials versus the US weighed on the Canadian dollar, while the Chinese yuan tumbled on concerns of capital flight and speculation for easier central bank policy should a full-blown trade war come to fruition.

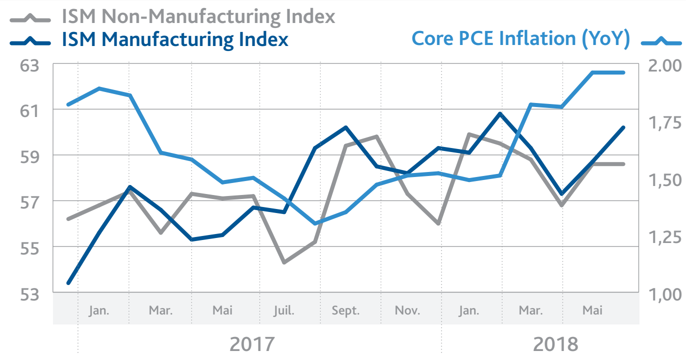
In commodity markets, crude prices blew through the $70-mark in late June as shrinking stockpiles and supply disruptions from Venezuela, Libya, and Canada compounded the anticipated plunge in Iranian production – which threatens to restrain global supplies at a time when global demand remains resilient. In contrast, gold prices retreated alongside the stronger US dollar, while copper got caught up in the US-China trade debacle and capped its largest monthly loss since March.



Despite ramped-up protectionist rhetoric from the Trump administration, business leaders remain upbeat on the fortunes for the Canadian economy. The Business Outlook Survey Indicator rose to its highest level since 2011, while firms appear poised to boost both hiring and investment to meet increased demand.

CANADA

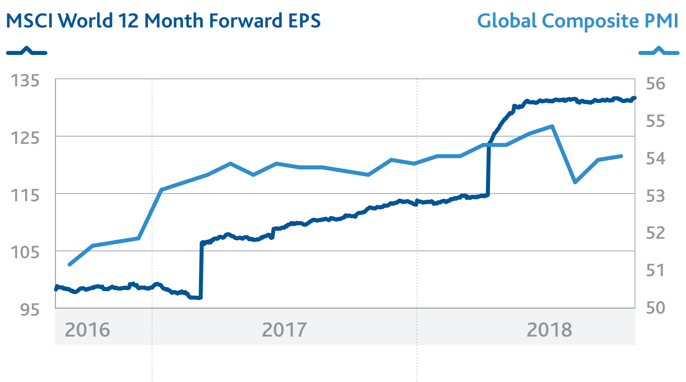
While the downside risks to the Canadian economy have indeed increased alongside a deterioration in US trade relations, the economy managed to eke out a small gain in April - thanks to a rebound in both the manufacturing and real estate sectors. Despite the persistent stalemate in NAFTA talks, Canadian firms remained upbeat during the second quarter, with both hiring and investment intensions remaining firmly in positive territory – while corporations described overall business conditions as "buoyant" in general. Furthermore, inflation expectations also shifted higher, with 2/3 of firms expecting inflation to come in above 2.0% - all of which should provide the Bank of Canada with the confidence to raise interest rates in July.



Confidence remains elevated on both the manufacturing and services sides of the US economy, reflecting the broad based nature of the acceleration in general. Meanwhile, core PCE inflation hit the Federal Reserve's 2% target for the first time in 6 years – all but cementing the case for two more rate hikes in 2018.

USA

The US economy is firing on all cylinders. The mighty consumer continues to thrive on the combination of a tighter labour market, rising wages, and lower taxes – all of which has helped to cushion the blow from higher gasoline costs. Meanwhile, the factory sector also regained some momentum and has proven fairly resilient to the highly contentious trade backdrop - suggesting that while tariff anxieties are indeed building, aggregate business conditions remain reasonably robust. Taken together, growth is set to rebound strongly in the second quarter, while the Federal Reserve's preferred inflation gauge is sitting right on target for the first time since April 2012 – all but reaffirming the Federal Reserve's projections for two more rate hikes this year.



While the risks to the global outlook have indeed increased since the beginning of 2018, the good news is that the fundamental backdrop remains reasonably bright - with little sign of vulnerability in growth and earnings prospects at this time.

INTERNATIONAL

While the world economy has shifted gears somewhat in 2018, global growth conditions remain healthy in general. The European economy is reverting back towards more sustainable (albeit above-trend) levels, justifying the ECB decision to cease its asset purchases at year end. And in Japan, exports have accelerated for two straight months even after newly-imposed steel and aluminum tariffs, while the Chinese economy has held up fairly well even despite the intensifying global trade dispute and a deleveraging campaign at home. That being said, risks to the outlook have arguably increased – most notably on the trade front, while the prospect for tighter global monetary policy, emerging market vulnerability, and geopolitical uncertainty also warrants some caution at this time.

Our current scenarios are for a synchronized global expansion (50%), which is a continuation of the current environment that benefits equities, trade protectionism (30%), which would be negative for equities and positive for bonds, geopolitical instability (10%) that would introduce significant financial market volatility, and finally, stronger than expected growth & inflation (10%) which would be negative for bonds and positive for equities.

MAIN SCENARIO
SYNCHRONIZED GLOBAL EXPANSION

PROBABILITY 50%

The global economy continues to grind higher in a synchronous manner, with all major regions contributing to the advance. The US leads the global charge, thanks to widespread momentum across both the consumer and manufacturing space, while the double-dose of fiscal stimulus boosts an already-buoyant economy. Meanwhile, the Canadian economy moderates towards a more sustainable, albeit above-trend pace – though the fate of NAFTA clouds the outlook. Finally, policymakers in Europe and Japan ultimately prove successful in reflating growth, while emerging market economies prosper in the environment of improving global demand, ample liquidity, and rising commodity prices. Taken together, the lucrative combination of synchronized global growth and a revival in commodity prices should bolster inflation expectations across the world, though not to levels that would threaten the status of the economic recovery. This reflationary backdrop bodes well for equities and commodities (ex-gold) at the expense of fixed income and the US dollar.

SCENARIO 2
TRADE PROTECTIONISM

PROBABILITY 30%

The biggest risk to our base case scenario is a rise in protectionism stemming from the US and the threat of a trade war that would derail the synchronous global expansion. Specifically, President Trump's rhetoric on protectionism has translated into action ahead of the midterm elections, with the US imposing tariffs on a variety of imports including solar panels, washing machines, steel, and aluminum – which have been met with retaliatory measures from some of America's closest allies in response. However, Mr. Trump has upped the ante by threatening to slap tariffs on an additional $200 billion of imports from China as well as auto imports – which would be detrimental for trade flows and the global economy alike. In this scenario, anti-trade rhetoric in the US becomes a reality and results in tariffs being imposed on economies such as China, Canada, Europe, Japan and Mexico, with further retaliation igniting a full-blown global trade war.

SCENARIO 3
GEOPOLITICAL INSTABILITY

PROBABILITY 10%

Political upheaval in Europe and vulnerabilities in the emerging world could ignite a crisis in confidence – disrupting the global economy and financial markets alike. Specifically in Italy, the Five Star and League parties have formed a coalition government with Eurosceptic tendencies, with plans to expand fiscal policy that would go against the fiscal rules and threaten the relationship with the European Union – which risks throwing the region into political disarray at the same inopportune time that a lack of progress in Brexit negotiations has raised the odds of a "hard Brexit" scenario. Meanwhile, emerging market economies remain susceptible to a strengthening greenback, particularly those countries with high levels of external debt. An increase in debt-servicing costs raises default risks and capital outflows for the weaker links, with the potential for contagion to spread more broadly across the developing world.

SCENARIO 4
STRONGER GROWTH & INFLATION

PROBABILITY 10%

Inflation expectations de-anchor from current subdued levels and surge higher on the back of the stronger-than-expected global growth backdrop. Specifically, the global expansion has become increasingly self-sustaining and excess capacity has been absorbed, with all major OECD economies operating at/near full potential. When combined with central bank's tolerance for higher inflation and the overly-stimulative monetary policy backdrop in general, the global economy could potentially overheat and trigger a faster tightening schedule as central bank doves morph into hawks - increasing the risk of a policy error, shortening the cycle, and stifling the economic recovery. With asset valuations at extreme levels, this leaves little room for error from a financial market perspective.

FORECASTS FOR THE NEXT 12 MONTHS

SCENARIOS	JUNE 29, 2018	SYNCHRONIZED GLOBAL EXPANSION	TRADE PROTECTIONISM	GEOPOLITICAL INSTABILITY	STRONGER GROWTH & INFLATION
PROBABILITY		50%	30%	10%	10%
GDP GROWTH (Y/Y)					
Global	3.50%	4.00%	2.00%	3.00%	4.25%
Canada	2.50%	3.00%	0.50%	1.00%	3.25%
U.S.	2.80%	3.50%	1.00%	1.00%	4.00%
INFLATION (HEADLINE Y/Y)					
Canada	2.20%	2.25%	1.50%	1.50%	3.00%
U.S.	2.80%	2.25%	2.00%	1.75%	3.25%
SHORT-TERM RATES					
Bank of Canada	1.25%	2.00%	1.00%	1.25%	2.50%
Federal Reserve	2.00%	3.00%	2.00%	2.25%	3.25%
10-YEAR RATES					
Canada Government	2.17%	2.85%	1.40%	1.70%	3.80%
US Government	2.86%	3.25%	2.25%	2.00%	4.25%
PROFIT GROWTH (12 MONTHS FORWARD)					
Canada	9.5%	10.2%	-26.5%	-16.0%	12.8%
U.S.	15.1%	16.4%	-17.9%	-7.6%	16.4%
EAFE	12.2%	8.2%	-22.7%	-18.8%	15.9%
EM	21.2%	26.9%	-17.5%	-17.5%	33.2%
P/E (FORWARD 12 MONTHS)					
Canada	15.6X	16.5X	16.5X	16.5X	16.0X
U.S.	16.2X	16.5X	16.5X	17.0X	18.0X
EAFE	13.5X	15.0X	15.0X	14.5X	15.0X
EM	11.2X	13.0X	11.0X	12.5X	12.5X
CURRENCIES					
CAD/USD	0.76	0.83	0.65	0.70	0.85
EUR/USD	1.17	1.20	1.10	1.00	1.10
USD/JPY	110.76	110.00	100.00	100.00	120.00
COMMODITIES					
Oil (WTI, USD/barrel)	74.15	75.00	50.00	50.00	85.00

MATRIX OF EXPECTED RETURNS

SCENARIOS	SYNCHRONIZED GLOBAL EXPANSION	TRADE PROTECTIONISM	GEOPOLITICAL INSTABILITY	STRONGER GROWTH & INFLATION
PROBABILITY	50%	30%	10%	10%
Money Market	1.6%	1.1%	1.3%	1.9%
Canadian Bonds	-2.3%	7.9%	6.2%	-8.7%
Canadian Equity	6.4%	-29.0%	-18.9%	5.7%
U.S. Equity	-5.3%	-14.7%	-8.2%	0.8%
International Equity	-1.6%	-10.3%	-15.4%	2.9%
Emerging Market Equity	11.5%	-21.7%	-17.4%	9.9%

CURRENT STRATEGY [1]

	MINIMUM	BENCHMARK	MAXIMUM	STRATEGY	ALLOCATION	RELATIVE	DEC. 6 CHANGES
Money Market	0.0%	5.0%	25.0%	Overweight	20.0%	+15.0%	Increased by 10.0 %
Canadian Bonds	20.0%	40.0%	60.0%	Underweight	25.0%	-15.0%	No change
Canadian Equity	20.0%	25.0%	45.0%	Overweight	30.0%	+5.0%	Decreased by 2.5%
U.S. Equity	3.0%	13.0%	23.0%	Underweight	8.0%	-5.0%	Decreased by 5.0%
International Equity	2.0%	12.0%	22.0%	Underweight	7.0%	-5.0%	No change
Emerging Markets Equity	0.0%	5.0%	15.0%	Overweight	10.0%	+5.0%	Decreased by 2.5%

[1] Based on a 100 basis point value added objective. The benchmark employed here is based on a model portfolio and for illustrative purposes only. Individual client benchmarks are employed in the management of their respective portfolios.

FIERA CAPITAL

EVOLUTION OF STRATEGY[1]

	MONEY MARKET	CANADIAN BONDS	CANADIAN EQUITY	U.S. EQUITY	INTERNATIONAL EQUITY	EMERGING MARKETS EQUITY
August 10, 2011	+5.0%	-15.0%	+5.0%	+5.0%	0.0%	0.0%
October 5, 2011	+7.0%	-15.0%	+8.0%	0.0%	0.0%	0.0%
October 12, 2011	+6.0%	-10.0%	+4.0%	0.0%	0.0%	0.0%
November 11, 2011	+5.0%	0.0%	0.0%	0.0%	-5.0%	0.0%
December 7, 2011	0.0%	0.0%	+5.0%	0.0%	-5.0%	0.0%
April 20, 2012	+15.0%	-20.0%	+10.0%	0.0%	-5.0%	0.0%
July 31, 2012	+20.0%	-15.0%	0.0%	0.0%	-5.0%	0.0%
November 9, 2012	+10.0%	-15.0%	+10.0%	0.0%	-5.0%	0.0%
February 19, 2013	+5.0%	-15.0%	+10.0%	0.0%	0.0%	0.0%
August 6, 2013	0.0%	-15.0%	+10.0%	+5.0%	0.0%	0.0%
December 3, 2013	+10.0%	-15.0%	+5.0%	0.0%	0.0%	0.0%
February 5, 2014	0.0%	-15.0%	+10.0%	+10.0%	-5.0%	0.0%
October 14, 2014	0.0%	-20.0%	+5.0%	+10.0%	+5.0%	0.0%
November 14, 2014	+10.0%	-20.0%	+2.5%	+2.5%	+5.0%	0.0%
July 13, 2015	0.0%	-20.0%	+7.0%	+4.0%	+9.0%	0.0%
October 19, 2015	0.0%	-20.0%	+11.0%	+0.0%	+9.0%	0.0%
June 24, 2016	+9.0%	-20.0%	+11.0%	+0.0%	+0.0%	0.0%
July 12, 2016	0.0%	-20.0%	+15.0%	+0.0%	+0.0%	+5.0%
July 27, 2016	+5.0%	-20.0%	+12.5%	+0.0%	+0.0%	+2.5%
October 31, 2016	0.0%	-20.0%	+12.5%	0.0%	0.0%	+7.5%
April 5, 2017	+5.0%	-15.0%	+7.5%	0.0%	-5.0%	+7.5%
December 6, 2017	+15.0%	-15.0%	+5.0%	-5.0%	-5.0%	+5.0%

[1] Based on a 100 basis point value added objective.

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